Office of Property Disposal

Environmental Insurance: A Risk Management Tool For Contaminated Property

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Environmental insurance is a necessary part of many contaminated property transactions. It allows the risk associated with a contaminated site to be quantified as a manageable business risk—not as a "deal breaker," providing a valuable risk management negotiation tool. Insurance policies address known and unknown contamination. Although the Federal Government is self-insured, environmental insurance may be purchased by other parties involved in a Federal property transaction including lenders, developers, and local governments.

Although the Federal Government does not purchase insurance or pay for it for other parties, its use may assist local governments or private parties and allow a contaminated property deal to reach a successful conclusion.

Examples of transactions suitable for environmental insurance:

- Sale or purchase of real property
- Development of real property
- Lease of real property
- Financing of real property

Bottom Line...

Environmental insurance can:

- Improve marketability and allow a buyer to obtain financing for the property
- Quantify the environmental risk associated with the property
- Provide financial stability for the cleanup—essentially making the property as attractive as a "greenfield"
- Reduce risk, especially for unexpected costs

Downside...

Insurance is only as good as the provider. Therefore, it is important to identify a financially stable provider in light of the long-term liabilities associated with the transaction. Environmental insurance is limited in time and to the other coverage terms of the policy. Policies typically contain a number of exclusions that must be considered when evaluating the long-term cleanup responsibilities.

GSA

Improving Marketability

- The Comprehensive Environmental Response Compensation & Liability Act (CERCLA) requires the Federal Government to return and clean up the property if additional contamination is found after transfer. However, investors fear that this will result in excessive delays and stall redevelopment of the property. Insurance can provide an extra assurance that funding for the cleanup will be provided quickly and that the project will remain on schedule.
- General liability insurance policies typically do not cover owners of real property for environmental risks.
- Most environmental policies allow multiple parties (e.g., purchasers, lenders, sellers, and tenants) to be added to the policy providing assurances to those parties and assisting in the transaction.
- Lenders, in turn, feel more comfortable lending against a site that has a policy ensuring adequate funding for a timely and thorough cleanup response.

Why Buy Environmental Insurance?

Environmental insurance can provide coverage for:

- ✔ Business or work stoppage resulting from discovery of pollution
- ✔ New contamination discovered after acquiring the property
- ✔ Remediation expenses exceeding original cost estimate
- ✔ Claims against third-parties associated with ongoing operations
- ✔ Failure of the initial remedy before transfer
- ✔ Natural resource damages
- ✔ Claims against third-parties conducting remediation activities

Application to Federal Real Property Transactions

- Local governments, a major recipient of federal property, are usually not aware of the availability and utility of these products. It is important therefore, when structuring and negotiating a contaminated property deal, that they be apprised of the environmental insurance option.
- Insurance providers sometimes perform other services as part of the policy development process (i.e., site assessments, risk assessments, and cleanup cost estimates) which can be helpful in quantifying the risk of the property.
- In some Federal transferee policies, the insurance company has waived its right of subrogation against the Federal Government. This is important because generally, after the insurance company pays a claim, it seeks reimbursement from another party. Through a waiver of subrogation, the insurance company agrees not to sue the Federal Government for damages or costs incurred.
- Environmental insurance may be particularly useful in “early transfers” where the transferee will conduct the cleanup of the property. It is not however, limited to those types of transactions. Although environmental insurance can assist an early transfer transaction, it will not eliminate the Federal Government's liability for the contamination.

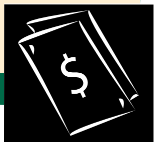
Insurance Policies

Names of policies differ by provider. The three most common variations are listed below:

- **Cleanup Cost Cap or Stop Gap**—This type of policy covers the insured for costs in excess of the approved remediation plan, i.e., remediation cost overruns. The policy pays up to an agreed upon amount when the costs of the remediation plan are exceeded. The policy can be structured to include coverage for offsite cleanup costs on surrounding properties. The coverage typically runs until the cleanup is completed.
- **Pollution Legal Liability**—This type of policy is designed to cover on- or off-site claims against the current or previous owner for bodily injury or property damage arising from cleanup activities. It is possible to obtain coverage for known and unknown pre-existing contamination. This type of coverage can be used either before or after the cleanup is conducted. Another option typically available under a pollution legal liability policy is coverage for business interruption as a result of newly discovered contamination.
- **Property Transfer**—This policy is designed to cover claims arising on real property for unknown, pre-transfer contamination and existing known contamination below reportable levels. This type of insurance has a number of similar coverage options as the pollution legal liability, but has additional elements that deal with the actual transfer of the property. Typically, parties to the transaction, e.g., the seller, buyer, and lender, can all be included on the property transfer insurance policy.

Cautionary Note: Current policies do not provide protection for UXO and radiological and biochemical wastes, and some policies will not cover lead-based paint or asbestos. It is important to understand the limitations associated with the coverage options and the scope of all exclusions contained in the policy.

Each of these types of policies may be purchased separately or combined with another type of insurance policy, depending upon the nature of the deal.



Coverage Options

- **Claims-Made**—If the insured is covered on a claims-made basis, claims can only be made during a set policy period. For example, if the insured was covered for the year of 2002, the claim would have to be made in that year. The insured in some cases can purchase extended coverage. This is the more common of the two.
- **Occurrence-Based**—An occurrence-based policy covers the insured for future, undiscovered contamination. The coverage is measured by when the event actually occurs not when the claim is filed. Therefore, as long as the event took place during the policy period, coverage is still provided if the claim is filed after the policy period has expired. For example, if the insured was covered for the year 2002 and an event covered under the policy occurred in that year, the event would still be covered even if its discovery did not occur until a subsequent year.

Policy and Deductible Ranges

Generally, the price of insurance is driven by the level of site characterization, the nature of the constituents of concern, the nature of the reuse (e.g., whether residential or industrial), the terms of the policy and limits of liability, and the expected costs of remediation.

- Policy coverage ranges typically from $1 million to $100 million depending on the options purchased under a particular plan.
- Deductibles typically run anywhere from as low as $5,000 to $2 million.
- Premiums frequently can range from $1,500 to $10,000 per year.

Where can I find general information on environmental insurance?

Appendix from *Improving Access-to-Capital, Site Transition, and Brownfield Redevelopment Programs Through More Effective Environmental Risk Management—Insurance for the Non-Specialist:*
http://www.epa.gov/commonsense/repins.htm

HUD's Environmental Insurance for Brownfield's Redevelopment: A Feasibility Study:
http://www.huduser.org/publications/econdev/envins.html

Environmental Insurance: Tools to Manage Environmental Liabilities:
http://www.enviroglobe.com/insure/

Environmental Insurance for Brownfield Sites:
http://www.enviroglobe.com/brownfields/Insurebrown.htm

US EPA's Environmental Insurance Products for Brownfields Cleanup and Redevelopment
http://www.epa.gov/brownfields/html-doc/Insurance.htm

DoD's Using Environmental Insurance in DoD Property Transfers: A New Tool for Managing Cleanup Risk
http://www.dtic.mil/envirodod/brac/ei_factsheet.pdf

*Environmental Insurance Providers**

As a result of the demand for environmental insurance and the increase in understanding of the environmental risks associated with contaminated property, several insurance companies now provide coverage for certain environmental risks. Below, you will find some examples of companies in this field:

- AIG Environmental
- United Capitol Insurance Company
- Zurich-American Insurance Company
- Seneca Insurance
- ECS, an XL Capital Company
- Kemper Environmental
- Gulf
- Chubb

*The reference to specific providers is meant solely for informational purposes and is not an endorsement.